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UNITED STATES GENERAL ACCOUNTING OFFICE

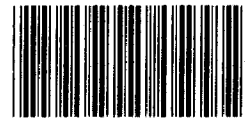
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TESTIMONY OF
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COMPTROLLER GENERAL OF THE UNITED STATES
BEFORE THE
SUBCOMMITTEE ON LEGISLATION AND NATIONAL SECURITY
COMMITTEE ON GOVERNMENT OPERATIONS
HOUSE OF REPRESENTATIVES
ON
THE BALANCED BUDGET AND EMERGENCY
DEFICIT CONTROL ACT OF 1985



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Mr. Chairman and Members of the Subcommittee:

I am pleased to appear before the Subcommittee on a matter of great importance—namely, doing something to bring under control our chronic budget deficits and enormous national debt. I fully share the concern and frustration that have led to the measure now being considered by the Subcommittee, commonly

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referred to as the "Gramm-Rudman Amendment." Something must be done soon, in the form of spending cuts, revenue increases, or both, to put the federal government's fiscal house in order.

OUR PREFERENCE FOR A SUBSTANTIVE
RATHER THAN MECHANISTIC SOLUTION

While sharing the basic fiscal goal of "Gramm-Rudman," we would as a general rule prefer a more substantive—and less mechanistic—solution. Instead of making program-specific reductions, the amendment lays out a time-table and formula for achieving a balanced budget by fiscal year 1991. Included are provisions that would require the President to make cutbacks, subject to certain limitations specified in the amendment, in the event that regular congressional-presidential actions on the budget produce insufficient deficit reductions.

Our concern is that such an approach has potential for generating added controversy over spending decisions, and producing unanticipated effects on programs and the economy. This is not to say that the potential problems, which I will briefly discuss, outweigh the possible benefits of the amendment. Rather, we are urging that the Congress examine certain matters while further considering Gramm-Rudman. Depending upon the results of this additional examination, the Congress may choose to refine Gramm-Rudman, adopt a substantially different approach, or accept it in its present form.

DISCRETIONARY FEATURES COULD GENERATE
ADDITIONAL CONTROVERSY

While the amendment is notable for its overall formula approach, it contains some ambiguities and room for discretionary actions. Discretionary actions by the President or Director of OMB could figure prominently in triggering the automatic cutbacks, and following that, in determining which activities are included in a list of cutbacks as well as the kind of cutback treatment that is applied. For

example, which civil and defense contracts would be identified for cuts? The methodology used by executive branch officials for computing contract modifications penalties would be important in this regard, as would their interpretations of the government's legal obligations under those contracts.

Similarly, there would be some room for interpretation as to which programs are "indexed directly," and which ones shall be categorized as "controllable." Is Medicare indexed directly? The placement of programs into one or the other of these categories would determine the kind of cutback action that could be taken. Recent floor debates in the Senate show a large degree of uncertainty on this question.

IMPOUNDMENT IMPLICATIONS

I would also like to comment on the possible impoundment implications of the amendment. Generally, action by the President to withhold funds from obligation is an impoundment, governed by the Impoundment Control Act and required to be reported, unless independent statutory authority exists for the withholding. Gramm-Rudman is just such independent authority. It permits withholdings and, as long as the President complies fully with the conditions imposed by Gramm-Rudman on such withholdings, the Impoundment Control Act has no application. Presidential withholdings would not require impoundment messages and actions by the Congress.

However, if the President invokes the authority of Gramm-Rudman to withhold funds but does not fully comply with its strictures, the result is arguably an impoundment which, if not reported by the President, is to be reported by us. For example, Gramm-Rudman prohibits the sequestration of funds if the result would be the elimination of a program. A sequestration which arguably had the effect of eliminating a program would be unauthorized by Gramm-Rudman and could be characterized as a de facto unreported impoundment.

Disputes over the scope or meaning of terms in Gramm-Rudman could also lead to the invocation of the Impoundment Control Act. For example, the President is supposed to sequester funds only for "controllable expenditures." If a sequestration applied to funds which in our view did not fall within the definition of controllable expenditures, it would arguably be an unreported impoundment.

In short, we expect that the ambiguities of the amendment's procedures would lead to numerous disputes over the propriety of presidential actions. This, in turn, could generate a significant amount of litigation and Impoundment Control Act actions.

On a related technical matter, we note that an earlier version of the amendment said that both the President's orders to suspend or modify laws relating to automatic spending increases, and his power to sequester funds for controllable expenditures were to be issued "notwithstanding the Impoundment Control Act." In the most recent version, however, it is only the suspensions and modifications which are explicitly "notwithstanding the Impoundment Control Act." We have so far found no indication why this change was made. While we suggest restoring the earlier language, we do not believe that the effect of the change is to subject sequestrations to the Act. Gramm-Rudman establishes a precise and carefully structured procedure; there is no room in the bill for the concurrent application of impoundment procedures.

POSSIBLE UNANTICIPATED EFFECTS ON THE CAPACITY OF
THE GOVERNMENT TO DELIVER DESIRED SERVICES AND AIDS

Another matter concerns the possible unanticipated effects of the amendment upon the capacity of the government to deliver services and other benefits. Until there is a better understanding of, and agreement on, the programs to be categorized as "indexed directly" and "controllable," we will be hampered in

predicting just where the budget cuts are likely to occur, and in what degree of severity. We only know that some kinds of outlays would be more "shielded" from cutbacks than others, forcing a certain concentration of the cuts.

This funneling effect of the cutbacks would start with the total shielding of the payments of Social Security Act's old-age, survivors, and disability insurance programs; the total shielding of payments of interest on the public debt; and some undetermined degree of shielding of payments on prior-year obligations, which are disproportionately high in the defense area. The payments in these areas in fiscal year 1984 totalled about \$477 billion, or about 56 percent of total governmental outlays. Additionally, there would be a total shielding of billions of non-COLA dollars in programs that are "indexed directly," such as Veterans Pensions or Railroad Retirement.

The result is that the cutbacks would fall disproportionately upon "controllable" budget accounts having relatively few prior year contracts and obligations. This could be a general salaries and expenses account for an agency such as the Federal Aviation Administration, the National Park Service, or the Federal Bureau of Investigation. In these kinds of accounts, heavy cuts could impair the capacity of the agencies to perform the services expected by the Congress and the Public. Some analysis should be made of the potential cutbacks that could affect such "typical" accounts.

ECONOMIC UNCERTAINTIES

An additional feature that should be of concern as the Congress debates this proposal is the degree of flexibility that Congress will have in dealing with a future deterioration in the economic environment. The amendment adopted by the Senate recognizes the need to be concerned about the economic environment by requiring the directors of OMB and CBO to report their forecasts of economic growth along with their forecasts of the budget deficit. However, only one

procedural change is introduced when the directors forecast a recession. That change is a 16-day extension of the time available to the President before he is required to institute the automatic spending reductions.

The amendment contains no provisions for changing the deficit targets of the current or subsequent years when a recession is forecast and provides no mechanism for adjusting the fiscal policy of the government if a recession develops, whether or not that recession was accurately forecast. In effect, the measure establishes a particular fiscal policy for the government for each of the next five fiscal years. An alternative fiscal policy can be adopted only if the President and the Congress agree through subsequent legislation to modify the deficit targets contained in this legislation.

BUDGET DISCIPLINE CONSIDERATIONS

A final matter we would like to raise concerns budget discipline implications. While the central aim of the amendment is to restore budget discipline, in the sense of restoring a sound fiscal policy, it paradoxically poses some direct or indirect challenges to another kind of budget discipline—i.e., making decisions through a unified budget that fully discloses programs' budgetary information on a consistent basis. We see some problems in this regard.

We may expect that program proponents will attempt to devise means of isolating their programs from possible cutback actions. The temptation to attempt to "game" the procedures will be almost irresistible, and the Congress should be alert to this likelihood. I am referring to such things as:

- revising contract language and penalty provisions to put contracts "off-limits;"
- signing contracts with outlays planned for subsequent years;
- obtaining legislation to place non-indexed programs on an indexed basis;

- passing legislation removing programs from the unified budget; and
- resorting to more "backdoor" spending methods.

Let me add some additional comments on two of the above items. On the unified budget matter, the amendment would essentially remove the Social Security programs previously mentioned from the unified budget. We defer to the Congress as to the wisdom of exempting Social Security from actions to reduce the deficit, but do not believe that shielding Social Security requires separating it from the unified budget. Separation would obscure the total financial condition of the government. As an alternative, we would urge the Congress to consider changing the current budget treatment of Social Security by requiring that the unified budget show separate subtotals for the revenues, expenses and surplus or deficit in the Social Security and non-Social Security accounts.

Finally , we would alert the Congress to the amendment's incentives for expanded "backdoor" spending. The mechanics of the amendment's automatic deficit reduction features operate on the spending side of the budget. This could easily promote efforts to isolate programs from possible cutbacks by switching to indirect, backdoor financial methods that would permit the programs to be classified as non-spending programs. There might be expanded uses of "tax expenditures" and "monetary credit" to accomplish this. The Congress should be cognizant of this possibility as it considers amendments such as this one.

Thank you Mr. Chairman. This concludes my prepared statement. I would be glad to answer any questions you or other members of the Subcommittee may have.

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